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**DIRECTORATE OF
INTELLIGENCE**

Intelligence Memorandum

The Economic Situation In Cambodia

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June 1971

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CENTRAL INTELLIGENCE AGENCY
Directorate of Intelligence
June 1971

INTELLIGENCE MEMORANDUM

The Economic Situation In Cambodia

Highlights

1. Price data compiled by US Embassy sources reflect substantial increases for April, casting some doubt on the validity of the official index, which indicates that food prices in the capital declined an average of 1% for the month as a whole.

2. The government has been unable to stem the rising tide of public concern over prices. Government officials, as well as the general public, place most of the blame for price increases on speculation by the Chinese merchants. Overt attacks on the Chinese have resulted in a number of shop closings, which has aggravated the shortage of goods and pushed prices even higher.

3. The black market value of the riel depreciated drastically in a wave of speculation during May. The price of the dollar in Phnom Penh stood at about 230 riels at the end of the month, compared with 140 riels on 10 May.

4. No action has yet been taken by the National Assembly on the 1971 budget submission, but allocations voted so far this year, if projected for a full calendar year, would result in military expenditures 40% below the amount proposed in the budget. Present appropriations are probably insufficient to cover FANK salaries, particularly in view of a recently reported upswing in unauthorized recruitment.

Note: This memorandum was prepared by the Office of Economic Research.

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5. Current negotiations with General Minh, Commander of Military Region 3, may permit transport of raw rubber from Cambodian border plantations to South Vietnam for processing and export.

6. The first convoy of civilian trucks since 25 March traversed Route 4, from Kompong Som to Phnom Penh, in early May without incident, and by the end of the month occasional groups of civilian trucks were making the trip without military escort. Shipments of produce to the capital via Route 5, however, were probably severely curtailed as a result of a bridge interdiction and increased enemy harassment.

7. Severe fuel shortages in the capital during May resulted in a number of plant shutdowns and rationing of the city's electricity. The shortages were more the result of bureaucratic errors that resulted in the delivery of fuel assortments ill-suited to the needs of the moment rather than of any diminution in the quantities delivered. Fuel was also in short supply in Battambang after shipments from Thailand were temporarily disrupted by the changeover to US AID import financing procedures.

8. Charts on prices and currency outstanding; imports, exports, and foreign exchange reserves; and government borrowing from the Banque du Cambodge follow the text.

Discussion

Prices

9. Official prices indexes, prepared by the Cambodian Institute of Statistics, show that retail prices declined an average of 2% during April, while prices of food items alone declined an average of 1%. Cumulative figures for the first four months of 1971 show a 1% decline in the general price index, while the food price index indicates a 4% decline. The data contrast markedly with those for the period March to December 1970, which show increases in the general

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index and in the food price index of 49% 1/ and 82%, respectively.

10. A compilation of prices of selected food-stuffs from US Embassy sources, however, casts some doubt on the validity of the index (see the table). It shows that prices of certain items increased substantially during the first three weeks of April following a three-month period of relative stability. The cost of pork, lard, and fresh fish, which declined during the first quarter of the year, for example, had greatly increased by the third week in April, along with prices for beef, chicken, duck eggs, bananas, and fish sauce. Only prices for duck, dry fish, and vegetables show a decline for the three-week period.

11. Nevertheless, the food supply situation in the capital was very favorable during March and April. Deliveries of rice to Phnom Penh from Battambang, the major source of rice for the capital, were five times greater in both March and April than in any month since harvesting began last September. In fact, farm prices in Battambang reportedly rose for the first time in months as a result of the improved transportation situation. At the end of April, stocks of rice in the hands of Phnom Penh retail and wholesale merchants were the highest in several months.

12. No statistical information on prices in the capital is available for May, but price increases may have been substantial. Because of the unfavorable transport situation, quantities of meat and foodstuffs arriving in the capital were certainly far less than in either of the two previous months. Stock reports show that rice in the hands of Phnom Penh merchants declined substantially during the month. May also saw the beginning of sugar rationing in the capital as well as hoarding of hard-to-find items such as flashlight batteries.

1. A previous report, based on a publication of the Joint Chamber of Commerce, Agriculture and Industry, that the general price index showed only a 27% increase from March to December 1970 was in error.

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Prices of Selected Commodities in Phnom Penh

		Riels					
		1970		1971			
	Unit	March 2nd Week	December 4th Week	January 4th Week	February 4th Week	March 4th Week	April 3rd Week
White rice, No. 1	Kilogram	7	8	8	8	7	7
White rice, No. 2	Kilogram	6	7	7	7	6	6
Beef, filet	Kilogram	50	65	70	70	70	73
Beef, leg	Kilogram	31	45	50	50	50	53
Pork	Kilogram	53	105	107	101	96	106
Lard	Kilogram	41	90	100	87	77	80
Chicken	One	46	100	120	137	128	130
Duck	One	53	140	180	175	170	160
Chicken egg	One	2	5	5	5	5	5
Duck egg	One	3	5	5	5	5	7
Fish, fresh	Kilogram	22	43	35	32	35	39
Fish, dry	Kilogram	45	75	75	75	85	75
Vegetables	Kilogram	7	16	12	12	12	11
Green bananas	Kilogram	11	14	15	14	15	17
Ordinary bananas	Kilogram	3	7	7	7	7	8
Fish sauce	Bottle	20	22	22	22	22	23

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Public Reaction to Inflation

13. Public sensitivity to price increases was abundantly evident during May. A 30 May demonstration in the town of Oudong, Kandal Province, followed the pattern of earlier demonstrations in the towns of Battambang, Kampong Chhnang, Kampot, Siem Reap, and Svay Rieng. In each case, the participants were mostly students, but usually included a few soldiers dressed in civilian clothes. The demonstrations were targeted against merchants, especially the Chinese, who had not heeded earlier warnings to lower prices. Organizers, playing upon traditional Khmer antipathy toward the Chinese merchants, attributed the high prices to the merchants' greed. The demonstrations usually resulted in the destruction of shop stalls, looting, and sometimes burning. In no instance did the civilian authorities move to prevent or halt the demonstrations.

14. Phnom Penh officials have done little to ease public tension over rising prices. Their modest countermeasures included the publication of decrees fixing prices of some staples and requiring regular stock reports from merchants and warehouse operators. Steps have also been taken to supervise sales of fuel supplies, and a commission has been established to rationalize utilization of transport and to organize convoys.

15. It is all too evident that most government officials do not understand the causes of inflation and consider the economic situation to be amenable to easy solution. Like the general public, they tend to attribute price increases to such things as the "American" war tax, to VC/NVA efforts to disrupt the economy by flooding the market with riels, and especially to speculation by the Chinese merchant, who has long been regarded as acquisitive, unscrupulous, and the primary cause of Cambodia's economic ills. Attacks on the Chinese have only aggravated the shortage of commodities and pushed prices even higher. After the riots in Battambang, for example, few shops opened for business because shopkeepers could not operate at prices established by the students. In fact, many merchants were seeking to have their operating permits canceled for fear the government would force them to reopen.

SECRETBlack Market Currency Prices

16. The black market value of the riel depreciated drastically during May. The price of the dollar in Phnom Penh moved from about 140 riels on 10 May to approximately 276 riels on 20 May, and by the end of the month was still as high as 230 riels.

17. The wave of speculation probably was triggered by a combination of events. These include rumors of imminent devaluation of the riel, the Finance Minister's consideration of new controls on bank withdrawals, the arrival by air of "several tons" of newly printed riel notes, and police crackdowns on black market moneylenders.

18. At the root of Cambodia's precarious financial position, however, is the continuing monetary expansion that has been necessary to maintain the army. Currency in circulation increased 88% during 1970 and an additional 26% during the first five months of 1971. Since the Cambodians have moved very slowly in utilizing US AID funds, deliveries of aid goods, which had been expected to reduce substantially the size of Cambodia's budget deficit this year, will be far less than originally projected. With export earnings at only a fraction of prewar levels and reserves committed largely to debt servicing and to imports of essential items ineligible for US financing, Cambodia has insufficient foreign exchange reserves of its own to make up the shortfall in US AID deliveries.

1971 Budget

19. No action has yet been taken by the National Assembly on the 1971 budget submission, although the year is nearly half over. The extended delay has been attributed primarily to the leadership gap precipitated by the illness and resignation of Lon Nol. However, government operations have so far been funded with appropriations voted on a monthly basis. The amounts voted so far this year, if projected for a full calendar year, would result in total budget expenditures of about 14.0 billion riels, 7.1 billion riels for the civilian budget and 6.9 billion riels for the military.

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20. While projected civilian expenditures are consistent with the 1971 budget submission of 7.2 billion riels, projected military expenditures are not only far below the budget submission figure of 11.5 billion riels but also far below our own projection -- 9.0 billion riels -- calculated by deflating official estimates for overstatement of average military personnel costs. 2/

21. With appropriations at such a low level, the government probably has had to resort more than ever to the practice of delaying military payments. Several instances of troops not being paid -- some for as long as six months -- have been reported. It is difficult to determine, however, in a given instance whether the funds actually were not available or whether they were pocketed [REDACTED]

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22. In any case, delaying payments is only postponing the inevitable, and it is doubtful whether FANK can be supported much longer at present appropriation levels, particularly in view of a reported upswing in recruitment. The military budget projection is based on a FANK strength of 220,000 men, the maximum consistent with the US-Cambodian agreement. According to Phnom Penh, however, the FANK quartermaster directorate currently carries 245,000 on the payroll.

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SECRETImproved Prospects for Rubber Exports

24. Following recent South Vietnamese-Cambodian bilateral talks, Khmer economic negotiator Touch Kim told US Embassy officials that the South Vietnamese are ready to work out a formal agreement that would clear the way for transport of raw rubber from Cambodian border plantations to South Vietnam for processing and export. The agreement would cover processing fees and taxes, notably the amount of the so-called "patente" to be charged per kilogram of rubber processed.

25. Prospects for the export of some Cambodian rubber from plantations bordering South Vietnam were dimmed, at least temporarily, by the death of Do Cao Tri, former Commanding General of South Vietnam's Military Region 3

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[redacted] With official problems near resolution, the only remaining unknown is whether or not Tri's successor, General Minh, will accept Tri's bargain. Representatives of the Mimot plantation have already had an initial negotiating session with Minh and are said to have settled the question of fees, but Minh apparently has not yet decided to assume responsibility for the safety of rubber shipments.

26. A favorable decision might provide a rejuvenating spark to an industry that has been totally devitalized for over a year and would undoubtedly give an important psychological lift to the Khmer. Moreover, even a relatively small volume of rubber output would significantly improve Cambodia's prospective foreign exchange earnings for 1971, currently estimated at a meager \$14 million. By comparison, Cambodian exports of rubber alone were valued at about \$25 million in 1969. Tapping, of course, would be limited to the relatively few plantations in friendly hands, specifically those near Mimot and Krek.

Transport Security

27. Route 4 was reopened to military traffic on 1 May, and a week later the first convoy of

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civilian trucks since 25 March made the trip from Kompong Som to Phnom Penh without harrassment. The highway began to sustain regular traffic after temporary repairs were effected on a heavily damaged portion of the road in the Pich Nil Pass. It is not known whether permanent repairs, necessary to keep the section usable through the rainy season, have been made. A substantial portion of several hundred new vehicles stored at Kompong Som -- many of them Red Cross trucks and ambulances donated by Japan -- have already been transferred to Phnom Penh, along with supplies from the port's bulging warehouses. There were no reports of vehicles being fired upon, and by the end of the month occasional groups of civilian trucks were making the trip without military escort.

28. Khmer Communist elements remain active along the southern portion of the highway, however. During the last week of May, truck drivers reported that Khmer Communists in the vicinity of Prek Nop -- about 10 kilometers south of the intersection of Routes 4 and 3 -- had resumed taxation of trucks, a practice that was first reported in early March. Current tax rates reportedly range from only 300 to 600 riels per truck (equivalent to about \$5 to \$10 at the official rate), however, compared with alleged charges of up to 5,000 riels per truck (about \$90) in March.

29. Shipments of produce from Battambang to Phnom Penh via Route 5 were disrupted by the enemy's destruction on 2 May of a bridge 25 kilometers northwest of Kompong Chhnang near Baribour. Makeshift repairs put the bridge back into operation on 12 May, but two days later it collapsed under a heavily loaded truck and did not become operational again until 26 May. Because the bridge is located south of the rail head at Pursat, 3/ it carries all of the traffic between Phnom Penh and Battambang. A poorly constructed bypass permitted some traffic to continue through this point while the bridge was out of operation, but shipments of produce from the northwest were probably severely

3. *The Pursat-Phnom Penh section of the railroad has been inoperable since June 1970.*

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curtailed. Rail traffic between Battambang and Pursat also was disrupted when explosives derailed a train about 40 kilometers south of Battambang on 4 June.

30. Furthermore, the increased harassment of Route 5 that became apparent during the latter half of April remained unusually heavy throughout May and probably caused a sharp increase in truck rates, as well as increased transit times, as vehicle movements had to be organized into convoys under military escorts. In 11 separate instances of harassment of Route 5 traffic in May, at least 14 vehicles were destroyed or driven off, and others were fired upon. Most of the attacks occurred within 40 kilometers of Kampong Chhnang and were attributed to well-armed bands of Khmer Communists. The enemy was also active west of Route 5. On 5 May, five trucks carrying marble on Route 10 were burned 15 kilometers east of Pailin. Three days later a National Sugar Company camp in the same area was raided and a number of vehicles were stolen.

31. Kampot remained cut off from overland access to the rest of the country as a result of the destruction in April and May of numerous bridges on Route 3 east of its intersection with Route 4. Roads to the east and north of Kampot continued to be blocked by the presence of enemy troops. Consequently, the city has been receiving petroleum and other essential supplies by sea. Air freight and passenger traffic has increased markedly. Because of the interdictions, the cement plant at Chakrei Ting, 15 kilometers north of Kampot, has cut production back to about 150 tons a day, but there is no information as to whether its output is being moved by sea to Phnom Penh.

32. Three Mekong River convoys arrived in Phnom Penh under military escort during May. One convoy drew fire from enemy mortars, rockets, and machineguns from a point six kilometers south of the Route 1 ferry crossing. One tug and a freighter sustained slight damage.

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Petroleum Situation

33. Phnom Penh's petroleum reserves dwindled in May to critically low levels. Kerosine reserves were exhausted during the first week, and before the end of the month, reserves of industrial and auto diesel oils also reached zero, while motorists formed long lines at filling stations for the few remaining gallons of gasoline. Shortages of heavy fuels forced a number of industrial plants in the Phnom Penh area to curtail production, and the city's two powerplants had to ration power to avoid complete shutdowns. Some residential and commercial areas were without electricity for as long as 10 hours a day.

34. The shortages appeared to be due more to a failure to deliver the right assortment of fuels rather than to any significant decline in the volume of deliveries. Petroleum shipments to Phnom Penh via the Mekong in May approximated volumes delivered in earlier months, as shown in the following tabulation:

<u>Period</u>	<u>Metric Tons</u>
Total <i>a/</i>	53,400
17-31 January	5,500
February	10,000
March	11,300
April	10,000
May	10,600
1-10 June	6,000

a. During the period, additional amounts of petroleum were trucked into Phnom Penh from Kompong Som, Battambang, and Saigon. A complete accounting of the shipments is not available, but their cumulative total is believed to be less (possibly much less) than 5,000 tons.

The crisis was alleviated by the arrival of an unusually large shipment on 10 June. If present

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petroleum delivery schedules are implemented, the volume of fuels delivered to Phnom Penh in armed convoys in June may exceed 12,000 tons.

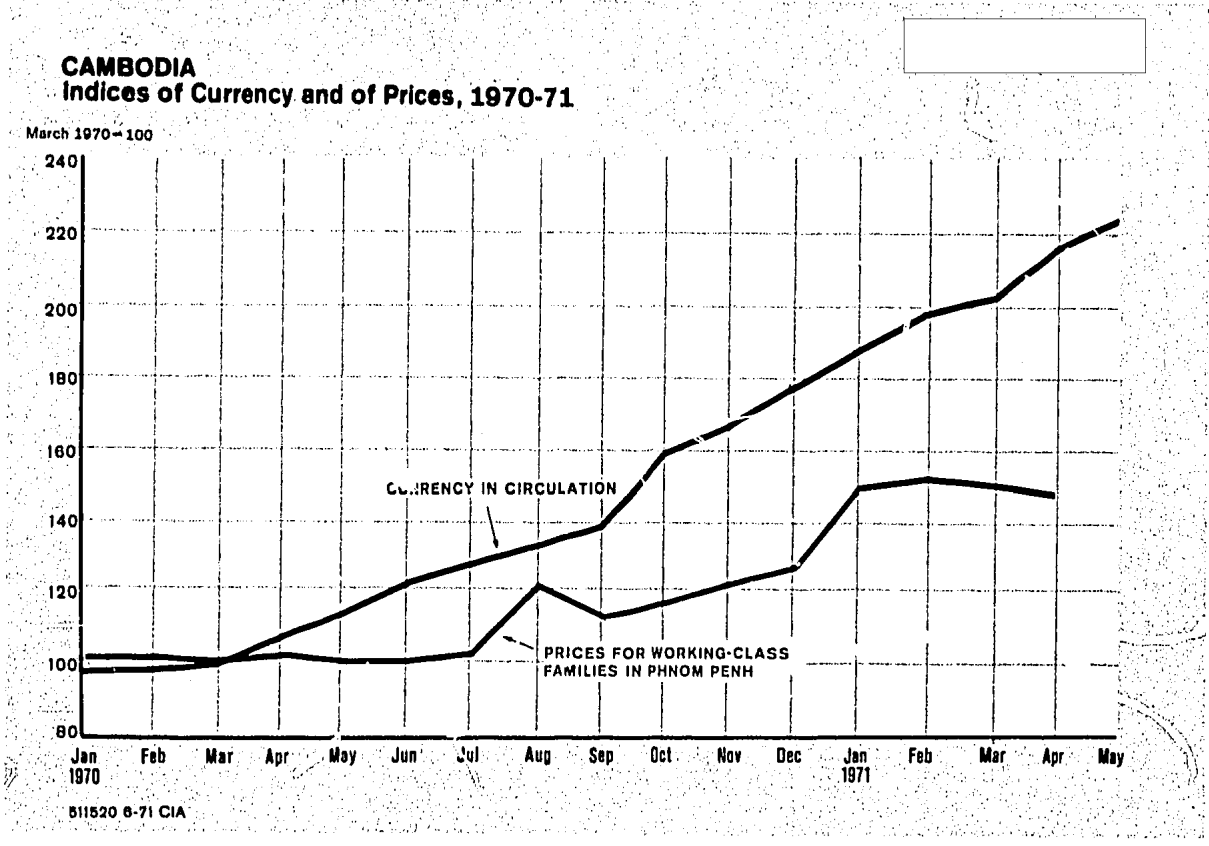
35. Petroleum deliveries to Battambang (via truck from Bangkok) declined sharply from mid-April through most of May, causing severe fuel shortages. Stringent rationing was imposed, and the price of gasoline on the black market rose to several times the official price. Truck transport rates were increased accordingly. The initial decline in deliveries was attributed to a strike by Thai drivers in protest over the heavy fine imposed on a Shell Company driver arrested for smuggling. The major cause of the disruption, however, was the development of new payment procedures for reimbursement of expenditures for petroleum imports from Thailand from US AID funds. Following the establishment of the new payment procedures in the second week of May, petroleum shipments from Shell Thailand -- the principal supplier -- picked up sharply and by the end of the month appeared to be back to normal.

36. There has been no further word as to whether the Cambodians plan to put the Kompong Som refinery back into operation or leave it idle.

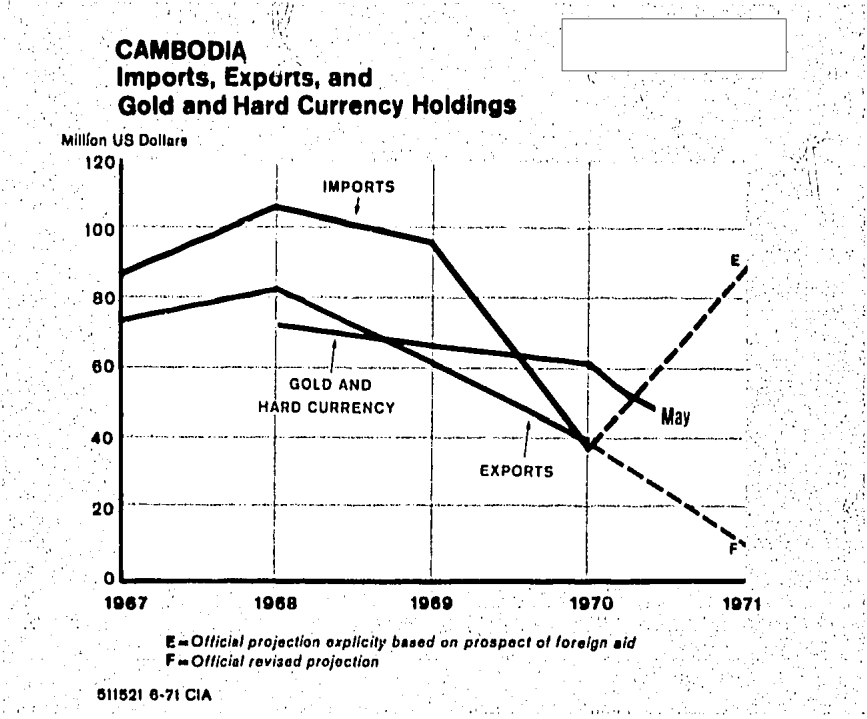
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